

## Zoomlion Heavy Industry - H (1157 HK)

### Dividend cut a surprise; Positive on the recovery story

Zoomlion's net profit in 2019 came in at RMB4.38bn, up 116% YoY, within the profit growth range of 113-123% YoY released in the profit alert earlier. That said, the Company unexpectedly proposed not to pay dividend (compared with 98% payout in 2018), in spite of its strong operating cash flow. We believe such move aims at protecting balance sheet and offers flexibility to buyback outstanding bonds. We fine-tuned our 2020E/21E earnings forecast -5%/-2% on lower revenue assumptions. Our TP is revised down to HK\$6.9, based on 1.1x 2020E P/B (down from 1.3x), on the back of 11.7%-12% ROE in 2020E-22E. Recovery of construction machinery demand in 2Q will serve as key catalyst.

- Key highlights on 2019 results.** The revenue growth in 2H19 was 50% YoY and gross margin expanded 1.3ppt YoY to 30% (stable HoH). However, S&D expense ratio increased to 9% in 2H19, compared with 8.3% in 2H18 and 8.4% in 1H19. Besides, R&D expense ratio increased to 5% in 2H19, up significantly from 2.7% in 2H18 and 2.1% in 1H19. We believe the higher expense ratio was due to the launch of new products. Thanks to lower finance expense and effective tax rate, net profit in 2H19 grew 55% YoY to ~RMB1.8bn.
- Dividend cut reflects the conservative approach taken by the Company.** We are surprised about the dividend cut as the Company generated strong operating cash flow of RMB6bn in 2019, though it spent RMB2.1bn on share buyback for employee share incentive scheme. The latest dividend policy suggested that the Company is potentially planning for debt repayment or redemption. Several tranches of bonds will be matured over the coming few years, with the first one in Dec 2022 (principal amount of US\$600m with coupon rate of 6.13%). The recent volatile bond market due to the lack of liquidity may offer the Company with the opportunity to buyback at discount.
- Risk factors:** (1) Unexpected weakness on property construction activities; (2) Slow recovery of infrastructure spending; (3) High earnings volatility.

#### Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	28,697	43,307	48,890	53,585	57,723
YoY growth (%)	39.3	50.9	12.9	9.6	7.7
Net income (RMB mn)	2,031	4,381	5,060	5,610	6,039
EPS (RMB)	0.27	0.58	0.64	0.71	0.77
YoY growth (%)	51.5	119.2	10.2	10.9	7.7
Consensus EPS (RMB)	n/a	n/a	0.66	0.74	0.69
EV/EBITDA (x)	12.1	7.8	6.7	6.1	5.8
P/E (x)	18.8	8.8	8.2	7.4	6.7
P/B (x)	1.0	1.0	0.9	0.8	0.7
Yield (%)	5.0	0.0	3.0	3.4	3.7
ROE (%)	5.4	11.4	12.1	11.9	11.7
Net gearing (%)	33.6	31.3	19.1	16.2	11.1

Source: Company data, CMBIS estimates

### BUY (Maintain)

Target Price	HK\$6.90
(Previous TP)	HK\$7.92
Up/Downside	+19%
Current Price	HK\$5.80

#### China Capital Goods

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#### Stock Data

Mkt Cap (HK\$ mn)	50,592
Avg 3 mths t/o (HK\$ mn)	48
52w High/Low (HK\$)	7.12/3.83
Total Issued Shares (mn)	<b>1,388 (H)</b>
	6,456 (A)

Source: Bloomberg

#### Shareholding Structure

SASAC of Hunan Province	16.0%
Management team	4.9%
A share free float	61.4%
H share free float	17.7%

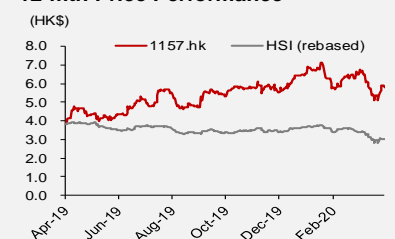
Source: HKEx, Shanghai Stock Exchange

#### Share Performance

	Absolute	Relative
1-mth	-10.2%	-11.3%
3-mth	-9.9%	-18.2%
6-mth	9.2%	-11.2%

Source: Bloomberg

#### 12-mth Price Performance



Source: Bloomberg

#### Auditor: KPMG

#### Related Reports

- China Construction Machinery Sector - Scenario analysis on the resumption of factory production – 10 Feb 2020
- China Construction Machinery Sector – Four structural drivers to extend the upcycle to 2020-21E – 27 Nov 2019
- Zoomlion (1157 HK, BUY) - Stock ownership plan to offer strong incentive to management – 18 Nov 2019

**Figure 1: 2019 results highlights**

YE Dec 31 (RMB mn)	2018	2019	Change (YoY)	2019E	A vs E	1H18	1H19	Change (YoY)	2H18	2H19	Change (YoY)
<b>Total revenue</b>	<b>28,697</b>	<b>43,307</b>	<b>50.9%</b>	<b>44,342</b>	<b>-2.3%</b>	<b>14,706</b>	<b>22,262</b>	<b>51.4%</b>	<b>13,991</b>	<b>21,045</b>	<b>50.4%</b>
Cost of sales	(20,923)	(30,314)	44.9%	(30,741)	-1.4%	(10,953)	(15,584)	42.3%	(9,970)	(14,730)	47.7%
<b>Gross profit</b>	<b>7,774</b>	<b>12,993</b>	<b>67.1%</b>	<b>13,602</b>	<b>-4.5%</b>	<b>3,753</b>	<b>6,678</b>	<b>77.9%</b>	<b>4,021</b>	<b>6,315</b>	<b>57.1%</b>
Other income	882	1,017	15.3%	682	49.1%	397	622	56.7%	485	395	-18.6%
S&D expenses	(2,379)	(3,780)	58.9%	(3,326)	13.7%	(1,213)	(1,881)	55.1%	(1,166)	(1,899)	62.9%
Administrative expenses	(2,063)	(2,693)	30.5%	(2,882)	-6.6%	(1,139)	(1,324)	16.2%	(924)	(1,369)	48.2%
R&D expenses	(581)	(1,516)	160.9%	(887)	70.9%	(197)	(461)	134.0%	(384)	(1,055)	174.7%
<b>EBIT</b>	<b>3,633</b>	<b>6,021</b>	<b>65.7%</b>	<b>7,189</b>	<b>-16.2%</b>	<b>1,601</b>	<b>3,634</b>	<b>127.0%</b>	<b>2,032</b>	<b>2,387</b>	<b>17.5%</b>
Net finance income/(cost)	(1,205)	(1,165)	-3.3%	(1,359)	-14.3%	(607)	(596)	-1.8%	(598)	(569)	-4.8%
Finance income	347	539	55.3%	385	39.9%	192	277	44.3%	155	262	69.0%
Finance expenses	(1,552)	(1,704)	9.8%	(1,745)	-2.3%	(799)	(873)	9.3%	(753)	(831)	10.4%
Other gains/(losses)	0	0	n/a	0	n/a	0	0	n/a	0	0	n/a
Share of profit of JV and associates	222	188	-15.3%	235	-20.0%	86	82	-4.7%	136	106	-22.1%
<b>Pretax profit</b>	<b>2,650</b>	<b>5,044</b>	<b>90.3%</b>	<b>6,065</b>	<b>-16.8%</b>	<b>1,080</b>	<b>3,120</b>	<b>188.9%</b>	<b>1,570</b>	<b>1,924</b>	<b>22.5%</b>
Income tax	(682)	(759)	11.3%	(1,559)	-51.3%	(217)	(540)	148.8%	(465)	(219)	-52.9%
<b>After tax profit</b>	<b>1,968</b>	<b>4,285</b>	<b>117.7%</b>	<b>4,506</b>	<b>-4.9%</b>	<b>863</b>	<b>2,580</b>	<b>199.0%</b>	<b>1,105</b>	<b>1,705</b>	<b>54.3%</b>
MI & discontinued operation	63	96	52.4%	45	113.0%	11	5	-54.5%	52	91	75.0%
<b>Net profit</b>	<b>2,031</b>	<b>4,381</b>	<b>115.7%</b>	<b>4,551</b>	<b>-3.7%</b>	<b>874</b>	<b>2,585</b>	<b>195.8%</b>	<b>1,157</b>	<b>1,796</b>	<b>55.2%</b>
D&A	837	867	3.6%	852	1.8%	412	394	-4.4%	425	473	11.3%
<b>EBITDA</b>	<b>4,470</b>	<b>6,888</b>	<b>54.1%</b>	<b>8,041</b>	<b>-14.3%</b>	<b>2,013</b>	<b>4,028</b>	<b>100.1%</b>	<b>2,457</b>	<b>2,860</b>	<b>16.4%</b>

Source: Company data, CMBIS

**Figure 2: 2019 segment breakdown**

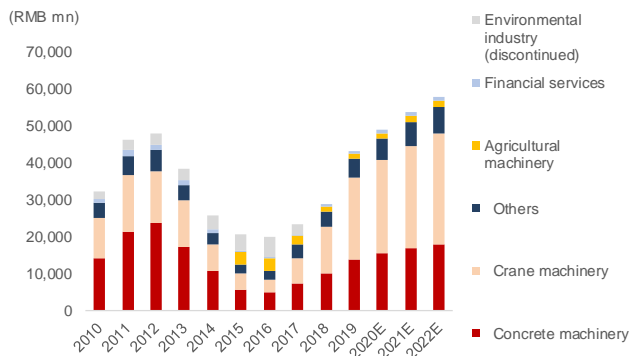
(RMB mn)	2018	2019	Change (YoY)	2019E	A vs E	1H18	1H19	Change (YoY)	2H18	2H19	Change (YoY)
<b>Revenue</b>											
Construction machinery	26,723	40,991	53.4%	42,348	-3.2%	13,578	21,017	54.8%	13,145	19,974	52.0%
Concrete machinery	10,165	13,902	36.8%	16,264	-14.5%	5,711	7,490	31.2%	4,454	6,412	44.0%
Crane machinery	12,472	22,147	77.6%	19,955	11.0%	5,651	11,005	94.7%	6,821	11,142	63.3%
Others	4,086	4,942	20.9%	6,129	-19.4%	2,216	2,522	13.8%	1,870	2,420	29.4%
Agricultural machinery	1,477	1,583	7.2%	1,447	9.4%	935	911	-2.6%	542	672	24.0%
Financial services	497	733	47.5%	547	34.1%	193	334	73.1%	304	399	31.3%
<b>Revenue (continuous operations)</b>	<b>28,697</b>	<b>43,307</b>	<b>50.9%</b>	<b>44,342</b>	<b>-2.3%</b>	<b>14,706</b>	<b>22,262</b>	<b>51.4%</b>	<b>13,991</b>	<b>21,045</b>	<b>50.4%</b>
Environmental industry (discontinued)	0	0	n/a	0	n/a	0	0	n/a	0	0	n/a
<b>Total revenue</b>	<b>28,697</b>	<b>43,307</b>	<b>50.9%</b>	<b>44,342</b>	<b>-2.3%</b>	<b>14,706</b>	<b>22,262</b>	<b>51.4%</b>	<b>13,991</b>	<b>21,045</b>	<b>50.4%</b>
<b>Gross profit</b>											
Construction machinery	7,176	12,193	69.9%	12,957	-5.9%	3,465	6,253	80.5%	3,711	5,940	60.1%
Concrete machinery	2,436	3,810	56.4%	4,717	-19.2%	1,265	2,050	62.1%	1,171	1,760	50.3%
Crane machinery	3,625	7,256	100.2%	6,585	10.2%	1,602	3,541	121.0%	2,023	3,715	83.6%
Others	1,115	1,127	1.1%	1,655	-31.9%	598	662	10.7%	517	465	-10.1%
Agricultural machinery	102	68	-33.3%	98	-30.9%	95	91	-4.2%	7	(23)	-428.6%
Financial services	496	732	47.6%	547	33.9%	193	334	73.1%	303	398	31.4%
<b>Gross profit (continuous operations)</b>	<b>7,774</b>	<b>12,993</b>	<b>67.1%</b>	<b>13,602</b>	<b>-4.5%</b>	<b>3,753</b>	<b>6,678</b>	<b>77.9%</b>	<b>4,021</b>	<b>6,315</b>	<b>57.1%</b>
Environmental industry (discontinued)	0	0	n/a	0	n/a	0	0	n/a	0	0	n/a
<b>Total gross profit</b>	<b>7,774</b>	<b>12,993</b>	<b>67.1%</b>	<b>13,602</b>	<b>-4.5%</b>	<b>3,753</b>	<b>6,678</b>	<b>77.9%</b>	<b>4,021</b>	<b>6,315</b>	<b>57.1%</b>
<b>Gross margin</b>			<b>Change (ppt)</b>		<b>Diff (ppt)</b>			<b>Change (ppt)</b>			<b>Change (ppt)</b>
Construction machinery	26.9%	29.7%	2.9	30.6%	-0.8	25.5%	29.8%	4.2	28.2%	29.7%	1.5
Concrete machinery	24.0%	27.4%	3.4	29.0%	-1.6	22.2%	27.4%	5.2	26.3%	27.4%	1.2
Crane machinery	29.1%	32.8%	3.7	33.0%	-0.2	28.3%	32.2%	3.8	29.7%	33.3%	3.7
Others	27.3%	22.8%	-4.5	27.0%	-4.2	27.0%	26.2%	(0.7)	27.6%	19.2%	(8.4)
Agricultural machinery	6.9%	4.3%	-2.6	6.8%	-2.5	10.2%	10.0%	(0.2)	1.3%	-3.4%	(4.7)
Financial services	99.8%	99.9%	0.1	100.0%	-0.1	100.0%	100.0%	0.0	99.7%	99.7%	0.1
<b>Gross margin (continuous operations)</b>	<b>27.1%</b>	<b>30.0%</b>	<b>2.9</b>	<b>30.7%</b>	<b>-0.7</b>	<b>25.5%</b>	<b>30.0%</b>	<b>4.5</b>	<b>28.7%</b>	<b>30.0%</b>	<b>1.3</b>
Environmental industry (discontinued)	-	-	n/a	-	n/a	n/a	n/a	n/a	n/a	n/a	n/a
<b>Average gross margin</b>	<b>27.1%</b>	<b>30.0%</b>	<b>2.9</b>	<b>30.7%</b>	<b>-0.7</b>	<b>25.5%</b>	<b>30.0%</b>	<b>4.5</b>	<b>28.7%</b>	<b>30.0%</b>	<b>1.3</b>

Source: Company data, CMBIS

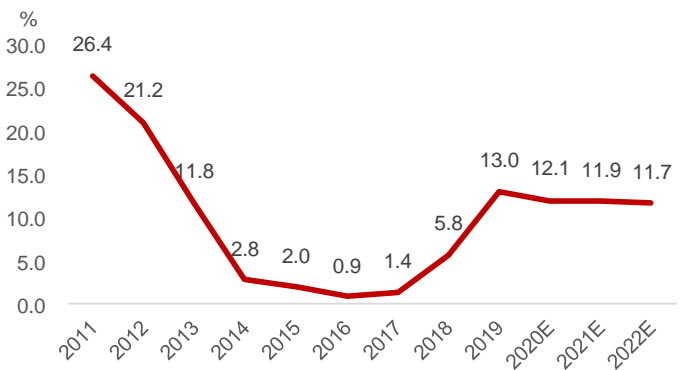
**Figure 3: Change in key assumptions**

	Old		New		Change	
	2020E	2021E	2020E	2021E	2020E	2021E
(RMB mn)						
<b>Revenue</b>						
Construction machinery	48,700	52,716	46,501	51,124	-5%	-3%
Concrete machinery	18,704	19,826	15,570	16,816	-17%	-15%
Crane machinery	22,948	24,784	25,248	27,772	10%	12%
Others	7,048	8,106	5,683	6,536	-19%	-19%
Agricultural machinery	1,447	1,476	1,583	1,615	9%	9%
Financial services	601	631	806	847	34%	34%
<b>Total revenue</b>	<b>50,749</b>	<b>54,824</b>	<b>48,890</b>	<b>53,585</b>	<b>-4%</b>	<b>-2%</b>
<b>Revenue growth</b>						
					<b>Change in ppt</b>	
Construction machinery	15.0%	8.2%	13.4%	9.9%	(1.6)	1.7
Concrete machinery	15.0%	6.0%	12.0%	8.0%	(3.0)	2.0
Crane machinery	15.0%	8.0%	14.0%	10.0%	(1.0)	2.0
Others	15.0%	15.0%	15.0%	15.0%	0.0	0.0
Agricultural machinery	0.0%	2.0%	0.0%	2.0%	0.0	0.0
Financial services	10.0%	5.0%	10.0%	5.0%	0.0	0.0
<b>Total revenue growth</b>	<b>14.4%</b>	<b>8.0%</b>	<b>12.9%</b>	<b>9.6%</b>	<b>(1.6)</b>	<b>1.6</b>
<b>Gross margin</b>						
					<b>Change in ppt</b>	
Construction machinery	30.4%	30.0%	29.6%	29.5%	-0.82	-0.49
Concrete machinery	29.0%	28.5%	27.3%	27.2%	-1.70	-1.30
Crane machinery	32.5%	32.0%	32.6%	32.5%	0.10	0.50
Others	27.5%	27.5%	22.7%	22.7%	-4.80	-4.80
Agricultural machinery	6.8%	6.9%	4.3%	4.3%	-2.50	-2.60
Financial services	100.0%	100.0%	100.0%	100.0%	0.00	0.00
<b>Average gross margin</b>	<b>30.6%</b>	<b>30.2%</b>	<b>30.0%</b>	<b>29.9%</b>	<b>-0.63</b>	<b>-0.32</b>

Source: Company data, CMBIS estimates

**Figure 4: Zoomlion's revenue trend**

Source: Company data, CMBIS estimates

**Figure 5: Zoomlion's ROE trend**

Source: Company data, CMBIS estimates

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Total revenue</b>	<b>28,697</b>	<b>43,307</b>	<b>48,890</b>	<b>53,585</b>	<b>57,723</b>
Cost of sales	-20,923	-30,314	-34,245	-37,586	-40,503
<b>Gross profit</b>	<b>7,774</b>	<b>12,993</b>	<b>14,646</b>	<b>16,000</b>	<b>17,220</b>
Other income	882	1,017	400	440	350
S&D expenses	-2,379	-3,780	-3,667	-4,019	-4,329
Administrative expenses	-2,063	-2,693	-3,178	-3,483	-3,752
R&D expenses	-581	-1,516	-978	-1,072	-1,154
<b>EBIT</b>	<b>3,633</b>	<b>6,021</b>	<b>7,224</b>	<b>7,866</b>	<b>8,335</b>
Net finance income/(cost)	-1,205	-1,165	-736	-662	-575
Finance income	347	539	358	409	389
Finance expenses	-1,552	-1,704	-1,094	-1,071	-964
Other gains/(losses)	0	0	0	0	0
Profit of JV and associates	222	188	254	271	288
<b>Pretax profit</b>	<b>2,650</b>	<b>5,044</b>	<b>6,742</b>	<b>7,475</b>	<b>8,048</b>
Income tax	-682	-759	-1,733	-1,921	-2,068
<b>After tax profit</b>	<b>1,968</b>	<b>4,285</b>	<b>5,009</b>	<b>5,554</b>	<b>5,979</b>
MI/discontinued operation	63	96	50	56	60
<b>Net profit</b>	<b>2,031</b>	<b>4,381</b>	<b>5,060</b>	<b>5,610</b>	<b>6,039</b>
<b>Recurring net profit</b>	<b>2,199</b>	<b>5,023</b>	<b>5,060</b>	<b>5,610</b>	<b>6,039</b>
D&A	837	867	884	916	934
<b>EBITDA</b>	<b>4,470</b>	<b>6,888</b>	<b>8,108</b>	<b>8,782</b>	<b>9,269</b>

### Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Pretax profit	2,650	5,044	6,742	7,475	8,048
Finance cost	1,451	1,704	1,094	1,071	964
Interest income	-347	-539	-358	-409	-389
Profit or loss of associates	-222	-188	-254	-271	-288
Disposal of PP&E/business	-152	0	0	0	0
Depreciation and amortization	837	867	884	916	934
Income tax paid	-431	-759	-1,733	-1,921	-2,068
Change in working capital	1,152	442	-1,933	-3,355	-2,591
Others	-221	-603	0	0	0
<b>Cash flow from operation</b>	<b>4,717</b>	<b>5,984</b>	<b>4,443</b>	<b>3,506</b>	<b>4,609</b>
Net capex on PP&E	-272	1,082	-1,046	-946	-600
Investment in JV/associates	-4	-301	0	0	0
Investment in subsidiaries	0	0	0	0	0
Investment in intangible assets	-103	-95	-100	0	0
Dividend received	4	0	0	0	0
Interest received	347	539	358	409	389
Others	-7,214	8,759	0	0	0
<b>Cash flow from investing</b>	<b>-7,242</b>	<b>9,984</b>	<b>-788</b>	<b>-537</b>	<b>-211</b>
Equity financing/(repurchase)	37	-2,145	1,074	0	0
Net bank borrowings	6,817	-14,008	-1,000	100	-4,100
Dividend paid	-1,308	-1,801	0	-1,265	-1,402
Interest paid	-1,428	-1,707	-1,094	-1,071	-964
Others	-16	13	0	0	0
<b>Cash flow from financing</b>	<b>4,102</b>	<b>-19,648</b>	<b>-1,021</b>	<b>-2,236</b>	<b>-6,467</b>
Change in cash	1,577	-3,696	2,634	733	-2,068
Cash at beginning of the year	7,148	8,754	5,073	7,707	8,441
Exchange and others	29	15	0	0	0
Cash at the end of the year	8,754	5,073	7,707	8,441	6,372

### Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Non-current assets</b>	<b>28,657</b>	<b>37,979</b>	<b>34,277</b>	<b>40,745</b>	<b>37,275</b>
PP&E	6,077	6,735	7,162	7,461	7,396
Lease prepayment	1,943	2,433	2,383	2,333	2,283
JV/associates	3,500	3,909	4,163	4,434	4,723
Financial lease receivables	3,656	7,771	5,088	8,419	6,131
Goodwill	2,046	2,017	2,017	2,017	2,017
Trade receivables	5,498	9,072	7,537	10,373	9,237
Intangible assets	2,153	2,043	1,927	1,708	1,489
Financial assets	2,379	2,644	2,644	2,644	2,644
Others	0	0	0	0	0
Deferred tax assets	1,276	1,271	1,271	1,271	1,271
Deposits	129	84	84	84	84
<b>Current assets</b>	<b>64,762</b>	<b>54,052</b>	<b>62,925</b>	<b>65,501</b>	<b>69,484</b>
Inventories	9,551	11,772	10,370	13,932	12,256
Trade & other receivables	21,554	20,839	26,846	25,124	31,176
Finance lease receivables	8,835	9,229	10,863	10,865	12,541
Financial assets at FVPL	13,787	4,311	4,311	4,311	4,311
Others	1,097	1,413	1,413	1,413	1,413
Pledged deposits	1,184	1,415	1,415	1,415	1,415
Cash	8,754	5,073	7,707	8,441	6,372
<b>Current liabilities</b>	<b>39,623</b>	<b>34,569</b>	<b>34,457</b>	<b>39,211</b>	<b>39,347</b>
Trade and other payables	15,786	25,012	24,713	28,834	28,870
Bank borrowings	22,044	7,312	7,112	7,212	7,312
Tax payable	151	186	186	186	186
Contract liabilities	1,602	1,934	2,321	2,855	2,855
Others	40	125	125	125	125
<b>Non-current liabilities</b>	<b>15,065</b>	<b>17,965</b>	<b>17,165</b>	<b>17,165</b>	<b>12,965</b>
Bank borrowings	13,645	14,515	13,715	13,715	9,515
Deferred tax liabilities	429	455	455	455	455
Others	991	2,995	2,995	2,995	2,995
<b>Equity</b>	<b>38,731</b>	<b>39,497</b>	<b>45,580</b>	<b>49,869</b>	<b>54,446</b>
Shareholders' equity	38,164	38,827	44,960	49,305	53,942
MI	567	670	620	564	505

### Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Sales mix (%)</b>					
Concrete machinery	35%	32%	32%	31%	31%
Crane machinery	43%	51%	52%	52%	52%
Others machinery	14%	11%	12%	12%	13%
Agricultural machinery	5%	4%	3%	3%	3%
Financial services	2%	2%	2%	2%	2%
Environmental (discontinued)	0%	0%	0%	0%	0%
Total	100%	100%	100%	100%	100%
<b>Profit &amp; loss ratio (%)</b>					
Gross margin	27.1	30.0	30.0	29.9	29.8
EBIT margin	12.7	13.9	14.8	14.7	14.4
Net profit margin	6.9	9.9	10.2	10.4	10.4
<b>Growth (%)</b>					
Revenue	39.3	50.9	12.9	9.6	7.7
Gross profit	80.6	67.1	12.7	9.2	7.6
EBIT	n/a	65.7	20.0	8.9	6.0
Core net profit	332.9	128.4	0.7	10.9	7.7
<b>Balance sheet ratio</b>					
Current ratio (x)	1.6	1.6	1.8	1.7	1.8
Trade receivable turnover days	342	240	240	238	240
Finance lease receivable turnover days	161	124	123	120	120
Inventory turnover days	161	128	118	118	118
Payable turnover days	268	246	265	260	260
Net debt / total equity (%)	33.6	31.3	19.1	16.2	11.1
<b>Profitability (%)</b>					
ROA	2.3	4.7	5.3	5.5	5.7
Core ROE	5.8	13.0	12.1	11.9	11.7
<b>Per share data</b>					
EPS (RMB)	0.27	0.58	0.64	0.71	0.77
Core EPS (RMB)	0.29	0.67	0.64	0.71	0.77
BVPS (RMB)	4.89	4.93	5.71	6.26	6.85
DPS (RMB)	0.25	0.00	0.16	0.18	0.19

Source: Company data, CMBIS estimates

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